

**CALIFORNIA BOARD OF ACCOUNTANCY**

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November 1, 2002

Dear Licensee:

Significant legislation related to the practice of public accountancy was enacted this year. Licensees must comply with these new laws when this legislation becomes effective on January 1, 2003.

To assist you in identifying the provisions that affect your practice, this letter provides a partial, limited summary of the new laws, as well as links to the bills so that you can read the full text of the new laws. You are strongly encouraged to read the laws that apply to you. You must not rely on this limited summary to determine compliance requirements. Further, related to most of the statutes referenced below, the Board is in the process of developing regulations to implement, interpret, and make specific their provisions.

Here are the key provisions:

▪ **Expanded Self-reporting Requirements — Business and Professions Code Section 5063** (AB 270, Chapter 231, pages 6-7).

In addition to self-reporting convictions of a crime related to the practice of public accounting or discipline by another licensing entity, commencing January 1, 2003, California CPAs and PAs also will be required to self-report the following:

- ✓ Any restatement of a financial statement by a client audited by the licensee.
- ✓ Any civil action settlement or arbitration award relating to the practice of public accountancy in which the amount of the settlement or award is \$30,000 or greater and when the licensee is not insured for the full amount.
- ✓ Any notice of the opening of a formal investigation of the licensee or a request for a Wells submission from the Securities and Exchange Commission.
- ✓ Any notice of the opening of an investigation by the federal Public Company Accounting Oversight Board.
- ✓ Any judgment entered against the licensee in any civil action alleging dishonesty, fraud, negligence, breach of fiduciary responsibility, embezzlement, theft, or other misconduct related to the licensee's professional practice.

A licensee is required to provide a signed, written report to the Board within 30 days of the date when he or she gains knowledge of the event. The report should set forth the facts which constitute the reportable event. The Board is in the process of developing

implementing regulations to provide additional guidance related to the self-reporting process.

- **New Requirement for Firms with Nonlicensee Owners — Business and Professions Code Section 5079** (AB 270, Chapter 231, page 9).

Commencing January 1, 2003, firms with nonlicensee owners will be required to disclose to their clients the actual or potential involvement of nonlicensee owners in the services provided.

The Board is in the process of developing regulations to clarify this requirement.

- **Additional cause for discipline — Business and Professions Code Section 5100(c)** (AB 270, Chapter 231, page 10).

Commencing January 1, 2003, repeated negligent acts by licensees, in the same or in different engagements, will be cause for discipline by the Board.

- **Audit Documentation — Business and Professions Code Section 5097** (AB 2873, Chapter 230, pages 2-3).

Section 5097 establishes specific audit documentation standards for all audits performed by California licensees (not only audits of publicly-traded companies). Commencing January 1, 2003, licensees must comply with the requirements of new Section 5097.

- ✓ Section 5097 defines audit documentation as a licensee's records of the procedures applied, the tests performed, the information obtained, and the pertinent conclusions reached.
- ✓ Audit documentation must be sufficiently complete so that a knowledgeable reviewer can examine the documentation and understand the audit procedures that were performed.
- ✓ If a procedure is not documented, it can be presumed that the work was not done. The burden of proving the work was done would then shift to the licensee.
- ✓ Audit documentation must be retained for a minimum of seven years and must be retained longer if required by professional standards or during the pendency of a Board investigation.
- ✓ Licensees must have written policies for documentation retention and destruction.

The Board is in the process of developing implementing regulations related to audit documentation and document retention/destruction policies.

- **Employment with the Audit Client — Business and Professions Code Section 5062.2** (AB 2970, Chapter 232, pages 1-2)

Licensees responsible for exercising significant judgment in the audit process are prohibited from accepting positions that would allow them to exercise significant authority over the accounting and auditing functions of a publicly-traded audit client for a 12-month period following issuance of the financial statement report.

- **New Requirement related to Commissions — Business and Professions Code Section 5061** (SB 1955, Chapter 1150, pages 25-27).

Reference: Corporations Code Section 164

Reference: California Code of Regulations, Title 2, Section 1896

Subdivision (c) of the amended commissions law prohibits licensees from providing services for a commission to the officers and directors of publicly-traded companies and other large for-profit audit clients and to the officers and directors of client-sponsored retirement plans. Section 5061 was also amended by AB 270; however, amendments in SB 1955 cancelled out those amendments. The Board is in the process of developing implementing regulations related to the changes in the commissions law.

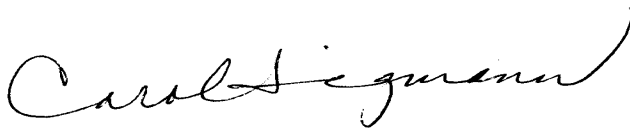
- **New Requirements for School District Auditors — Education Code Section 41020(f)** (AB 2834, Chapter 1128, pages 11-12).

The amended law requires the rotation of auditors after six consecutive years of auditing the same local educational agency (school district). This provision goes into effect July 1, 2003. If this requirement is a hardship for a local educational agency, the agency may request a waiver from the Education Audits Appeal Panel. AB 2834 has other provisions related to local educational agency audits. Therefore, affected licensees should review the entire text of the bill.

As indicated above in this letter, the Board is developing implementing regulations related to self-reporting, nonlicensee ownership, and audit documentation. The proposed regulations will be provided to you in the upcoming issue of **UPDATE**, scheduled for mailing in mid-January 2003.

A licensee who has concerns regarding the application of these new laws to his or her professional practice may wish to seek guidance from private legal counsel. The Board is not in a position to provide licensees with legal advice.

Sincerely,

A handwritten signature in cursive script, reading "Carol Sigmann".

Carol Sigmann  
Executive Officer